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Community and Regional Development

Budget function 450 covers federal programs that promote the economic viability of communities, encourage rural development, and assist in the nation's preparation for and response to natural and man-made disasters. The function includes spending for flood insurance, homeland security grants for state and local governments' first responders, the Community Development Block Grant program, disaster relief, credit assistance to help develop rural communities, and federal support for certain programs to assist Native Americans.

Spending for community and regional development was nearly flat from 1995 through 1998, with only modest growth in 1999 and 2000. In response to the September 11, 2001, terrorist attacks, the Congress significantly increased funding in this function for recovery efforts and grants to state and local first responders. Over $10 billion has been appropriated for such grants since 2003. Outlays for function 450 are expected to total $20.7 billion in 2005, an increase of about 75 percent since 2001. Near the start of this fiscal year, various disaster relief programs within the function received appropriations of $8.5 billion in response to three major hurricanes ($2 billion of that amount was provided at the end of fiscal year 2004). Outlays from that funding are likely to occur over several years.

Federal Spending, Fiscal Years 2000 to 2005 (Billions of dollars)

	2000	2001	2002	2003	2004	Estimate 2005	Average Annual Rate of Growth (Percent) 2000-2004	Average Annual Rate of Growth (Percent) 2004-2005
Budget Authority (Discretionary)	12.2	14.3	22.7	16.4	17.4	22.8	9.3	30.6
Outlays								
Discretionary	11.4	12.4	14.1	19.5	15.6	20.8	8.2	32.7
Mandatory	-0.8	-0.6	-1.2	-0.6	0.2	*	n.a.	n.a.
Total	10.6	11.8	13.0	18.9	15.8	20.7	10.4	31.2

Note: * = between -$50 million and zero; n.a. = not applicable (because some years have negative values).

450-01—Discretionary

Drop Wealthier Communities from the Community Development Block Grant Program

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-837	-850	-864	-882	-897	-4,330	-9,064
Outlays	-17	-285	-641	-769	-824	-2,536	-7,095

The Community Development Block Grant (CDBG) program provides annual grants to communities to help them aid low- and moderate-income households, eliminate slums and blight, or meet emergency needs by rehabilitating housing, improving infrastructure, and carrying out economic development activities. Part of the program—referred to as the entitlement component—makes grants directly to cities and urban counties. (The program also allocates funds to states, which distribute them to smaller and more rural communities—called nonentitlement areas—typically through a competitive process.) Funds from the entitlement component may also be used to repay bonds that are issued by local governments and guaranteed by the federal government under the Section 108 program. For 2005, the CDBG program received an appropriation of $4.1 billion, including $2.9 billion for entitlement communities.

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Under current law, the CDBG entitlement program is open to all urban counties, principal cities of metropolitan areas, and cities with a population of at least 50,000. The program allocates funds according to a formula based on population, the number of residents with income below the poverty level, the number of housing units with more than one person per room, the number of housing units built before 1940, and the extent to which population growth since 1960 is less than the average for all metropolitan cities. The formula does not require that a certain percentage of residents have income below the poverty level, nor does it exclude communities with high average income. An analysis in the President's 2004 budget showed that under that formula, population and other data from the 2000 census will shift funding from poorer to wealthier communities, as measured by average poverty rates.

This option would focus CDBG entitlement grants on needier areas and reduce funding accordingly. Several different changes to the current formula could yield similar results. One simple approach would be to exclude communities whose per capita income exceeded the national average by more than a certain percentage. For example, restricting the grants to communities whose per capita income was less than 112 percent of the national average would reduce entitlement funds by 26 percent, in part by eliminating grants to New York City and Los Angeles. To illustrate the general approach, this option would make a slightly smaller cut—20 percent of entitlement funding—which would save $2.5 billion over five years. (By comparison, the President's 2006 budget proposes to consolidate the CDBG program into a new economic and community development program to be administered by the Department of Commerce, in part to target federal funds toward needier areas.)

The main argument for narrowing eligibility for entitlement grants is that if the CDBG program can be justified at all—and some people contend that using federal funds for local development is inappropriate—its primary rationale is redistribution. In that case, redirecting money to wealthier communities serves no pressing interest.

The main argument against this option is that dropping wealthier communities from the CDBG program would reduce efforts to aid households in pockets of poverty within those communities, unless local governments reallocated their own funds to offset the lost grants.

RELATED OPTIONS: 450-04, 450-05, and 450-06

450-02—Discretionary

Convert the Rural Community Advancement Program to State Revolving Funds

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-12	-24	-38	-53	-67	-194	-4,517
Outlays	-1	-4	-12	-22	-33	-72	-2,372

The Department of Agriculture's Rural Community Advancement Program (RCAP) helps rural communities by providing loans, loan guarantees, and grants for water, waste-disposal, and waste-management projects; for community facilities; and for various activities to promote economic development. The program received appropriations of roughly $755 million in 2005 for grants and for the budgetary cost of its loans and loan guarantees. (That cost is defined under credit reform as the present value of interest rate subsidies and expected defaults on the loans and guarantees.) The President's 2006 budget proposes to reduce funding for the program to $522 million.

RCAP funds are generally allocated among states on the basis of their rural populations and their number of rural families with income below the poverty level. Within each state's allocation, the Department of Agriculture awards funds on a competitive basis to eligible applicants, including state and local agencies, nonprofit organizations, and (in the case of loan guarantees for business and industry) for-profit companies. The terms of a recipient's assistance depend on the purpose of the aid and, in some instances, on economic conditions in the recipient's area. For example, aid for water and waste-disposal projects can take the form of loans with interest rates ranging from 4.5 percent to market rates depending on the area's median household income. Areas that are particularly needy may receive grants or a mix of grants and loans.

This option would reduce future federal spending by providing money to capitalize state revolving funds for rural development and then ending federal assistance under RCAP. The amount of federal savings would depend on the level and timing of the contribution to capitalize the revolving funds. Under one illustrative approach, the federal government would provide funding of $755 million annually for five years to capitalize the funds, then cut off assistance in 2011. That approach would yield modest savings ($72 million) over five years but more-significant savings ($2.4 billion) through 2015. However, that level of capitalization would not by itself support the volume of loans and grants that RCAP now provides. Accordingly, the Congress could allow the revolving funds to use their capital as collateral with which to leverage additional financing from the private sector—as the state revolving funds established under the Clean Water Act and the Safe Drinking Water Act have been allowed to do.

The rationale for cutting off RCAP funding is that the federal government should not bear continuing responsibility for local development; rather, programs that benefit localities, whether urban or rural, should be funded at the state or local level. The rationale for the specific approach taken in this option is that a few years of federal funding to capitalize the revolving funds would provide a reasonable transition to the new policy.

One argument against converting RCAP to revolving funds is that states might change their types of aid (from grants to loans and from low-interest loans to high-interest loans) to avoid depleting the funds and to recoup the costs of any leveraged financing. Such a change could price the aid out of reach of needier communities. In addition, the estimated federal savings might not materialize: for example, the Congress has appropriated additional grants to the state funds for wastewater treatment systems after expiration of the original authorization for those grants.

RELATED OPTION: 300-13

450-03—Discretionary

Eliminate Region-Specific Development Agencies

						Total	
(Millions of dollars)	2006	2007	2008	2009	2010	2006-2010	2006-2015
Change in Spending							
Budget authority	-141	-143	-145	-149	-151	-729	-1,527
Outlays	-31	-75	-107	-128	-140	-481	-1,254

The federal government provides annual funding to three regional development agencies: the Appalachian Regional Commission (ARC), the Denali Commission, and the Delta Regional Authority. The ARC, established in 1965, conducts activities that promote economic growth in the Appalachian counties of 13 states, stretching from southern New York to northern Mississippi. Modeled after the ARC, the Denali Commission, which was created in 1998, covers remote areas in Alaska. Similarly, the Delta Regional Authority, established in 2000, covers 240 counties and parishes near the Mississippi River in eight states, stretching from southern Illinois to the Louisiana coast. For 2005, the Congress appropriated $65 million for the ARC, $68 million for the Denali Commission, and $6 million for the Delta Regional Authority. (The President's 2006 budget proposes cutting the Denali Commission's appropriation to $3 million.)

This option would discontinue federal funding for the Appalachian, Denali, and Delta regional development agencies. That change would reduce discretionary outlays by $31 million in 2006 and $481 million over five years.

The three agencies provide programs that are intended, among other things, to create jobs, improve rural education and health care, develop utilities and other infrastructure, and provide job training. Few studies have addressed the effectiveness of such programs. A 1996 report by the General Accounting Office (now the Government Accountability Office) reviewed the available research and found one study showing that counties aided by ARC programs grew significantly faster, according to various socioeconomic measures, than otherwise similar non-ARC counties. However, a strong link could not be made between the activities of the ARC and the counties' growth.

An advantage of ending federal funding for the three agencies is that it would shift more responsibility for supporting local or regional development to the states and localities whose citizens would benefit from that development. Another rationale for this option is that all parts of the country have needy areas; the Appalachian region, rural Alaska, and the Mississippi Delta should have no special claim to federal dollars. In that view, any federal development aid they do receive should come from nationwide programs, such as those of the Economic Development Administration, rather than from federal programs that focus on specific regions.

The main arguments against this option are that the federal government has a legitimate role to play in redistributing funds among states to support development in the neediest areas and that cutting federal funding would reduce local progress in education, health care, and job creation. Another argument is that Appalachia, rural Alaska, and the Mississippi Delta merit special attention because of their size, physical isolation, and severe poverty.

450-04—Discretionary

Eliminate the Neighborhood Reinvestment Corporation

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-116	-118	-120	-122	-124	-600	-1,257
Outlays	-116	-118	-120	-122	-124	-600	-1,257

The Neighborhood Reinvestment Corporation (NRC) is a public, nonprofit organization charged with revitalizing distressed neighborhoods. The NRC oversees a network of locally initiated and operated groups called NeighborWorks organizations (NWOs), which engage in a variety of housing, neighborhood revitalization, and community-building activities. The corporation provides technical and financial aid to start new NWOs; it also monitors and assists current ones. The NeighborWorks network includes over 220 member organizations operating in more than 2,500 communities nationwide. For 2005, the NRC received $114 million in appropriations.

This option would eliminate the Neighborhood Reinvestment Corporation, saving $116 million in 2006 and $600 million over five years.

With its appropriated funds, plus a few million dollars from fees and other sources, the NRC provides grants, conducts training programs and educational forums, and produces publications in support of NeighborWorks organizations. The bulk of its grant money goes to NWOs, which use the funds to purchase, construct, and rehabilitate properties; capitalize their revolving loan funds; develop new programs; and cover their operating costs. NWOs' revolving loan funds make mortgage and home improvement loans to individuals as well as loans to owners of mixed-use properties who provide long-term rental housing for low- and moderate-income people. In addition, the NRC awards grants to Neighborhood Housing Services of America, which provides a secondary market for the loans made by NWOs.

One rationale for eliminating the Neighborhood Reinvestment Corporation is that the federal government should not fund programs whose benefits are local rather than national. In addition, the NeighborWorks approach duplicates the efforts of other federal programs—particularly those of the Department of Housing and Urban Development—that also rehabilitate low-income housing and promote home ownership and community development. Moreover, the NRC is a relatively minor source of funding for NeighborWorks organizations. In 2003, its grants accounted for less than 20 percent of NWOs' funding from government sources and less than 5 percent of their total funding. Larger shares came from private lenders, foundations, corporations, and the Department of Housing and Urban Development.

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An argument against this option is that the large number of federal programs that exist to assist local development is evidence of widespread support for a federal role—particularly in areas where state and local governments may lack adequate resources of their own. Furthermore, NWOs address problems in whole neighborhoods rather than individual properties. And with their nonhousing activities (such as community-organization building, neighborhood cleanup and beautification, and leadership development), they provide economic and social benefits that other federal programs do not. Finally, the NRC may be particularly valuable because it has flexibility in making grants—which allows it to fund worthwhile efforts that do not fit within the narrow criteria of larger federal grantors—and because it provides the NWOs with needed training, program evaluation, and technical assistance.

RELATED OPTIONS: 450-01, 450-05, and 450-06

450-05—Discretionary

Eliminate the Community Development Financial Institutions Fund

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-52	-53	-54	-55	-56	-270	-566
Outlays	-5	-34	-50	-54	-55	-198	-488

The Community Development Financial Institutions (CDFI) Fund was created in 1994 to expand the availability of credit, investment capital, and financial services in distressed communities. Administered by the Treasury Department, the fund provides equity investments, grants, loans, and technical assistance to CDFIs, which include community development banks, credit unions, loan funds, venture capital funds, and microenterprise funds. In turn, those institutions provide a range of financial services—such as mortgage financing for first-time home buyers, loans and investments for new or expanding small businesses, and credit counseling—in markets that are underserved by traditional institutions. The CDFI Fund also provides incentive grants to traditional banks and thrifts to invest in CDFIs and to increase loans and services to distressed communities. In addition, the fund administers the New Markets Tax Credit (NMTC) program begun in 2002 to provide federal tax credits for qualified investments in "community development entities." The CDFI Fund received appropriations of $56 million for 2005.

This option would eliminate the CDFI Fund, reducing discretionary outlays by a total of $198 million through 2010. That estimate of savings takes into account the small amount of additional spending that would be required by other agencies to oversee the fund's existing loan portfolio and administer the NMTC program.

One rationale for doing away with the CDFI Fund is that local development should be financed at the state or local level, not by the federal government, since its benefits are not national in scope. Another argument is that the fund is redundant because many other federal programs and agencies—including the Empowerment Zones/Enterprise Communities Program, housing loan programs of the Rural Housing Service, the Community Development Block Grant program, the Neighborhood Reinvestment Corporation, and the Economic Development Administration—support home ownership and local economic development. Those programs and agencies received total funding of $4.7 billion for 2005. (The President's 2006 budget proposes consolidating the CDFI Fund into a new economic and community development program to be administered by the Department of Commerce.) Furthermore, assistance to CDFIs may be inefficient because it encourages loans that would otherwise not pass market tests for creditworthiness.

The primary argument against eliminating the CDFI Fund is that the federal government has a legitimate role in assisting needy communities, some of which lack access to traditional sources of credit. By helping existing CDFIs and stimulating the creation of others, the fund may provide an effective mechanism for leveraging private-sector investment with a relatively small federal contribution.

RELATED OPTIONS: 450-01, 450-04, and 450-06

450-06—Discretionary

Eliminate Grant Funding for Empowerment Zones

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-23	-23	-23	-25	-25	-119	-249
Outlays	0	-7	-18	-21	-23	-69	-195

The Omnibus Budget Reconciliation Act of 1993 authorized a 10-year program under which businesses would receive tax incentives—in the form of wage and tax credits, accelerated depreciation, and tax-exempt financing—to move to or expand in nine economically distressed communities designated "empowerment zones." To receive the designation, communities had to meet certain eligibility criteria and compete for selection on the basis of their strategic plans for implementing the program. When the law was enacted, the Congress provided $100 million in block grants for each urban empowerment zone and $40 million for each rural zone to support a broad range of economic and social development activities. The law also authorized the designation of 95 "enterprise communities" that were eligible for grants of $3 million each.

Since 1993, the Congress has authorized two additional rounds for designating empowerment zones; it has also authorized the designation of 40 "renewal communities," which are subject to a slightly different set of benefits. However, the program has increasingly emphasized tax incentives rather than grants. Only empowerment zones created in 1998 continue to receive grant funding. Neither Round III empowerment zones nor renewal communities ever received grants. In 2005, funding for grants to empowerment zones totaled $23 million, although the President had requested nothing.

This option would eliminate grant funding for empowerment zones and enterprise communities while leaving the tax incentives for those areas in place. That change would save a total of $69 million over five years.

The main arguments for this option are that tax breaks and other incentives are more effective than grants in promoting economic revival and that local development should be funded at the state or local level, not by the federal government, since its benefits are not national in scope. Furthermore, funds for social services and community benefits are available from a number of other government programs, including the Community Development Block Grant program and various regional commissions and authorities. (The President's 2006 budget proposes to consolidate the Empowerment Zones/Enterprise Communities Program into a new economic and community development program to be administered by the Department of Commerce.)

An argument against this option is that tax incentives alone are of limited effectiveness without related funding for publicity and technical assistance to local entrepreneurs. For example, the Government Accountability Office surveyed businesses operating in the nine original empowerment zones and found that they did not take advantage of many of the tax benefits available to them in tax year 1997 and that many did not know about some of those benefits. Finally, many communities have issued bonds and developed strategic plans expecting that multiyear grant funding would be available.

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RELATED OPTIONS: 450-01, 450-03, 450-04, and 450-05

450-07—Mandatory

Phase Out the Flood Insurance Subsidy on Pre-FIRM Structures Other Than Primary Residences

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Receipts	+14	+41	+55	+56	+56	+222	+513

The National Flood Insurance Program charges two different sets of premiums to insure buildings. One set applies to structures built either before 1975 or before the completion of a community's official flood insurance rate map (FIRM). Those structures are known as pre-FIRM buildings. The other set of premiums applies to post-FIRM buildings. Post-FIRM premiums are intended to be actuarially sound (that is, to cover the costs of all insured losses over the long term). They are based on a building's elevation relative to the flood level that is thought to have a 1 percent chance of being equaled or exceeded each year in that location. Pre-FIRM rates, by contrast, are heavily subsidized, on average, and do not take into account a building's elevation.

The Federal Emergency Management Agency (FEMA), which administers the flood insurance program, estimates that about 19 percent of coverage is provided at pre-FIRM rates. Those rates are available only for the first $35,000 of coverage for a one- to four-family dwelling and for the first $100,000 of coverage for a larger residential, nonresidential, or small-business building. Various levels of additional coverage are available at actuarially sound rates. The program also offers insurance for buildings' contents. As with the insurance for structures, policyholders in pre-FIRM buildings pay lower rates for the first tier of that coverage. FEMA estimates that the first-tier premiums for both buildings and contents equal 35 percent to 40 percent of the actuarial value of the insurance, implying subsidies of 60 percent to 65 percent. (Those figures are averages; the size of the subsidy for any particular building depends heavily on its elevation.)

This option would phase out the subsidy on all insured structures other than primary residences—in other words, on second and vacation homes, rental properties, and nonresidential buildings. That change would increase federal receipts by $14 million in 2006 and $222 million over the 2006-2010 period. Those estimates account for the likelihood that some current policyholders would drop their coverage. Flood insurance is mandatory only for properties that are located in special flood-hazard areas and that carry mortgages from federally insured lenders; and compliance with the requirement is far from complete. Thus, the Congressional Budget Office assumes that this option would reduce participation by both voluntary purchasers and property owners for whom the insurance was mandatory.

One argument for this option is that the subsidies in the flood insurance program have outlived their original justification as a temporary measure to encourage participation among property owners who were not previously aware of the magnitude of the flood risks they faced. According to that view, phasing out the subsidies would make pre-FIRM policyholders pay more of their fair share for insurance protection. A second rationale is that phasing out subsidies would give those policyholders incentives to relocate or take preventive measures. Keeping the subsidies for primary residences can be justified as focusing the subsidies on structures whose owners might face the greatest hardship in paying actuarial rates.

At least four arguments against phasing out subsidies for flood insurance can be made. First, charging full actuarial rates for properties built before FEMA documented the extent of local flood hazards could be considered unfair. Second, ending subsidies for rental properties might cause owners to pass on the increased costs to renters. Third, lower rates of participation in the program could lead to greater spending on federal disaster grants and loans, thus eroding some of the projected savings. Finally, the accuracy of the maps that FEMA uses to estimate the average long-term subsidy could be challenged on the grounds that premiums now roughly equal the average losses incurred to date for most pre-FIRM properties (except a few that flood repeatedly).

450-08—Discretionary

Restrict First-Responder Grants to Larger, At-Risk Communities

(Millions of dollars)	2006	2007	2008	2009	2010	Total 2006-2010	Total 2006-2015
Change in Spending							
Budget authority	-630	-640	-652	-663	-675	-3,260	-6,826
Outlays	-292	-489	-321	-644	-656	-2,403	-5,831

The Department of Homeland Security (DHS) issues grants to local governments to help police, firefighters, and other first responders prepare for terrorist attacks—by, for example, receiving biohazard training, acquiring special equipment (such as chemical suits), and providing additional physical security for critical infrastructure. For 2005, the Congress appropriated about $4 billion for those grants, which are administered by DHS's Office for State and Local Government Coordination and Preparedness. (The President's 2006 budget proposes reducing that funding by $420 million.) Currently, the grants are broadly available to communities of all sizes (through their state governments); indeed, most of the funds are distributed using a formula that guarantees that no state will receive less than 0.75 percent of the money. That approach may not fully reflect the relative attractiveness of communities as terrorist targets or the relative human and economic losses from an attack.

This option would reduce the funding to DHS for first-responder grants by 20 percent—or about $650 million annually—in order to limit the funding that would otherwise be available to small, low-risk communities. (The base for that 20 percent reduction would exclude about $900 million in grants that are specifically aimed at high-density, high-threat urban areas.) In addition, this option would alter the formula directing how first-responder grants are allocated so that support to large communities would not be affected. The revised formula could base eligibility not only on a community's population but also on whether it had significant national monuments or activities that were critical to the U.S. economy or to the provision of government services.

Proponents of changing the allocation formula argue that many grants now go to communities with small and dispersed populations, little critical economic activity, or few attractive targets for terrorists. Those communities may be less likely to be attacked and, if they were, would incur relatively small losses. Supporters of altering the formula also point out that not all the money currently available has been spent: as of September 31, 2004, more than $5 billion in prior years' funding had not yet been disbursed. And according to some observers, the dollars that were spent yielded little increase in national security, either because much of the spending did not benefit emergency preparedness or because it simply replaced other sources of funding for ongoing preparedness efforts. Legislation introduced in the previous Congress called for prioritizing grants to first responders on the basis of relative risk.

Opponents of changing the current allocation note that DHS already provides funds for other security programs (such as those at airports, seaports, and other transportation centers) that selectively benefit communities where risks of attack and losses may be greater. In addition, federal regulatory programs and private businesses are working to help protect attractive targets in those at-risk communities. Thus, opponents of this option argue, continuing to issue first-responder grants on the basis of geography may help restore balance in the allocation of funding. Moreover, terrorism is only one of many risks that communities face. Preparations nominally intended to deal with terrorist attacks may help mitigate the costs of crime, fires, storms, floods, or earthquakes—threats that exist everywhere. Advocates of that view support legislation that would broaden the uses for DHS's first-responder grants to include preparations for all types of disasters.

RELATED CBO PUBLICATIONS: *Federal Terrorism Reinsurance: An Update*, January 2005; *Homeland Security and the Private Sector,* December 2004; and *Federal Funding for Homeland Security*, April 2004